

Chief Financial Officer's Report to
Priorities and Finance Committee
2018 November 06

ISC: UNRESTRICTED
PFC2018-1125

2018 Triennial Reserve Review Report

EXECUTIVE SUMMARY

This report summarizes the results of the Triennial Reserve Review and the process performed by an Administrative Reserve Review Committee.

ADMINISTRATION RECOMMENDATION:

That the Priorities and Finance Committee recommends that Council:

1. Approve the changes to reserves as outlined in Attachment 1 and Attachment 2; and
2. Approve the list of reserves to be reviewed in 2019 as outlined in Attachment 3.

PREVIOUS COUNCIL DIRECTION / POLICY

The City Auditor's Office completed an audit of The City's Financial Reserves in 2009. The FCS2010-01 (AC2009-74) report dated 2010 January 18 detailed the recommendations of the audit and Administration's response and work plan to address the recommendations. One of Administration's responses was to create a Triennial Reserve Review process in which every reserve will be reviewed at least once every three years. The list of 18 reserves reviewed in 2018 was approved by Council (C2017-1123 Attachment 11.3) on 2017 December 18. Two other reserves were identified for follow-up in 2018 at the same time, and have been investigated as a part of this review.

On 2016 June 16, Council directed administration, through report TT2016-0204, to create a process to enable the CPA to access funds from the Parking Land Acquisition Reserve to support lifecycle requirements for existing cash-in-lieu parking facilities.

BACKGROUND

Reserves are part of good management that allows for funds to be either spent judiciously over time or to ensure service levels are maintained and not immediately impacted by downturns in the economy, adverse weather events, and other factors outside of The City's control. Reserves provide The City with the financial flexibility to react in a timely manner to the financial impacts of budget shortfalls and significant unexpected issues. A properly balanced approach to the planning and use of reserves is considered good financial management and is a key component of The City of Calgary's strong credit rating. For the majority of reserves, expenditures from and contributions to reserve funds are included in the Budget and Budget Adjustments approved by Council.

The City's open reserves consist of the following:

Reserve Type	# of Reserves	Reserve Balance as of 2017 Dec 31
Operating	16	\$695 million
Capital	17	\$884 million
Sustainment	12	\$624 million
Total per Reserve Report	45	\$2,203 million

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There are 16 operating reserves totalling \$695 million, of which \$574 million is held in the Fiscal Stability Reserve as an operating contingency fund and to provide for one-time funding. The majority of the 17 capital reserves totalling \$884 million are either fully committed or have substantial commitments against them to finance existing approved projects. A total of \$624 million is held in 12 separate sustainment reserves.

In 2010, Council approved Policy CFO013, Financial Reserves. The primary objective of the policy is to authorize or clarify processes required for:

- The creation of new reserves, including the purpose, funding, conditions, restrictions and appropriate minimum/maximum funding ranges;
- Administration of reserves, including annual contributions and withdrawals, investment income bearing status, the treatment of one-time or unanticipated revenue sources and courses of action if a reserve is over or under funded;
- Periodic reviews of all reserves; and
- Amendment or closure of a reserve.

Administration also developed and approved Administrative Policy FA-050, Financial Reserves, in support of the Council Policy. The Policy and associated procedures reflect best practices and provide additional guidance, procedures and responsibilities in the administration and reporting of reserves.

Council Policy CFO013 outlines a triennial review process requiring that every active reserve be reviewed at least once every three years.

The purpose of the Triennial Review process is to ensure that:

- i. Reserve activity meets all authorizing documents requirements;
- ii. Reserve activity is in accordance with City reserve policies and procedures;
- iii. The reserve's purpose, conditions and/or restrictions are still relevant; and
- iv. The reserve is still required in its current form.

The review for each active reserve will cover a period including the current year and the previous full year of operations for that reserve and shall be completed by an Administrative Reserve Review Committee comprised of:

- The Chief Financial Officer;
- Finance Manager, Corporate Budget Office;
- Finance Manager, Corporate Financial Reporting;
- A General Manager; and
- A Business Unit Director.

By the end of the year, the Administrative Reserve Review Committee prepares a report for the Priorities and Finance Committee. The report includes the criteria used to evaluate the reserves, a summary of all findings, any applicable recommendations based upon the findings, follow up of the previous year's review recommendations if required, and a list of reserves to be reviewed during the following year. The report's recommendations, and next year's review workplan, are subject to Council approval.

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INVESTIGATION: ALTERNATIVES AND ANALYSIS

In 2017, Council approved the 2018 review, consisting of 18 reserves. These represented a balance of \$965 million as of 2017 December 31, or approximately 44 percent of The City's total reserves balance.

1.0 Initial Review

A review team completed a detailed review of reserve transactions and documentation of each reserve. The review team collected all relevant reserve documents and reviewed selected 2016 and 2017 transactions in order to evaluate:

- Contributions from operations to reserves;
- Contributions from reserves to operations or capital;
- Transfers between reserves;
- Compliance of reserve activities with the reserve's mandate and all other City policies and procedures; and
- Completeness and accuracy of the disclosure of financial information in the Annual Reserve Report.

The review team provided findings to the Administrative Reserve Review Committee. The committee met several times throughout the year to consider the initial review results, evaluate recommendations made by the review team, determine whether the reserves are still relevant today, and whether they continue to align with current Council objectives.

2.0 Review Guiding Principles

Over the years, reserves have been created for a number of reasons and with various purposes. In order to consistently evaluate various types of reserves and determine whether changes should be recommended, the Administrative Reserve Review Committee previously agreed on a number of guiding principles.

2.1 Ensure clear separation between Reserves

The Administrative Reserve Review Committee recommends the consolidation or closure of reserves where multiple reserves serve similar purposes and to eliminate redundant reserves.

2.2 Business Categories

Currently, reserves are categorized according to the programs they support: operating, capital, or both operating and capital (sustainment). However, the Administrative Reserve Review Committee also categorized reserves by business purpose such that reserves can be evaluated consistently based on the business reason for the reserve. For example, some reserves have been created to manage the timing of cash flows. Such reserves should have a reserve plan and transactions should be budgeted wherever possible, but they do not necessarily lend themselves to a target balance.

Alternatively, reserves created for contingency purposes should have a target balance. Not all transactions for these reserves can be budgeted since Administration can not anticipate a contingent event, but establishing a target balance based on an estimate of risk is appropriate.

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2.3 Ongoing relevance of Reserves

The Administrative Reserve Review Committee also looked to ensure that the business reason for the reserve was still relevant and where applicable, that Administration has a plan on the strategic use of the reserve going forward and that reserve activity be budgeted where applicable.

3.0 Results of the Reviews

For the past several years, Administration has been following a number of control measures, such as annual checklists and documentation protocols, which have improved reserve processes and oversight.

3.1 Reserve activity meets all authorizing documents requirements

All reserves reviewed are being administered as intended. There were a few instances where authorizing document requirements are no longer relevant and have been replaced with alternate processes. Refer to Attachment 1 for further information.

3.2 Reserve activity is in accordance with City reserve policies and procedures

Almost all reserve activity reviewed was recorded in a timely fashion and in accordance with Council and Administrative reserve policies and Administrative reserve procedures. A one-time contribution of \$919,000 was made to the Snow and Ice Control (SNIC) Reserve from another internal budget that is not a typical funding source, and a minor restatement is required to the totals in the Corporate Housing Reserve and Downtown Improvement Fund. Aside from these, there were no issues identified with recorded reserve activity. Refer to Attachment 1 for further information and recommendations to address these issues, and to Attachment 2 to view the proposed restatements.

3.3 The reserve's purpose, conditions and/or restrictions are still relevant

The reserves' purposes, conditions and/or restrictions are still relevant. There are instances where a reserve's purpose, conditions and/or restrictions are recommended for update. Refer to Attachment 1 for further information and recommendations, and to Attachment 2 to view the proposed changes.

3.4 The reserve is still required

As part of the review, the Administrative Reserve Review Committee questions whether every reserve being reviewed is needed, or can be closed. The Parking Land Acquisition Reserve is recommended for immediate closure and replacement with a new reserve solely for the use of the Calgary Parking Authority, as per Council's direction in TT2016-0204. The LED Street Light Re-Lamping Reserve is recommended to cease funding after 2018 and closed once its balance has been depleted, expected by the end of 2019.

Refer to Attachment 1 for a complete list of general comments and reserve recommendations.

Attachment 2 includes reserve summaries from the 2017 Annual Reserve Report for the reserves reviewed. Suggested changes to the text are highlighted in red. Strikethrough text is to be removed.

Attachment 3 includes the list of reserves to be reviewed in 2019.

All three Attachments require Council approval.

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Stakeholder Engagement, Research and Communication

All relevant reserve leads and the Administrative Leadership Team were informed and consulted as part of the review.

Strategic Alignment

The Triennial Reserve Review process helps The City become a more effective organization by ensuring its reserves are being managed properly and effectively.

Social, Environmental, Economic (External)

A number of reserves reviewed support social and environmental programs which assist The City in providing such services. Proper management of the reserves helps The City maintain its commitment to these social and environmental initiatives.

Financial Capacity

Current and Future Operating Budget:

In certain instances, some reserve transactions are a result of unplanned activities (for example, use of contingency funds) and therefore cannot be budgeted. However, where reserve activities can be planned, those transactions are included in the operating budget. There is no impact on the current operating budget resulting from this report.

Current and Future Capital Budget:

Where reserve activities can be planned, those transactions are included in the capital budget. There is no impact on the current capital budget resulting from this report.

Risk Assessment

The Triennial Reserve Review process helps to mitigate risk by ensuring reserve balances are neither too high, where cash is held unnecessarily, or too low, where funds are insufficient to meet future needs. Maintaining adequate liquidity in the reserve system enables The City to respond quickly and effectively to shortfalls and unanticipated or uncontrollable events, improving corporate resiliency and reducing the risk that service levels might be adversely affected by economic trends and unforeseen circumstances. Strong reserves preserve Council and Administration's flexibility, and the vital role they play in preserving The City's fiscal stability is recognized by our credit rating agencies.

REASON(S) FOR RECOMMENDATION(S):

The recommendations help to streamline administration of reserves and, where required, update reserve purposes, conditions and restrictions to Council and the general public.

ATTACHMENT(S)

1. Attachment 1 – Reserve review comments and recommendations
2. Attachment 2 – Relevant excerpts from the 2017 Annual Reserve Report
3. Attachment 3 – Reserves to be reviewed in 2019